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IN THE

Supreme Court of the United States

OCTOBER TERM, 1940.

No. 419.

GUY T. HELVING, COMMISSIONER OF INTERNAL REVENUE,

Petitioner,

vs.

MARY M. HUTCHINGS,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT.

SUPPLEMENTAL BRIEF FOR RESPONDENT.

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By leave of the Court, the Respondent respectfully requests permission to file this its Supplemental Brief. This request is made due to the fact that Petitioner's Brief was not received by Respondent until the afternoon of January 1st, which was subsequent to the time Petitioner's Brief was filed.

SUMMARY OF ARGUMENT.

POINT I.

The tax is not imposed upon the receipt of the property by the Donee but is an excise tax upon the act of the Donor in making a transfer of the property.

POINT II.

The "Apprehended Difficulty" of determining the number of Donees and the amount they received is not present in this case.

ARGUMENT.

POINT I.

The tax is not imposed upon the receipt of the property by the Donee but is an excise tax upon the act of the Donor in making a transfer of the property.

The gist of the Petitioner's argument in the case of **United States vs. Pelzer**, No. 393, this term, which the Petitioner adopts as argument in this case, appears to be based entirely upon the theory that instead of the tax here in question being a tax measured by the value of the gift made by the Donor, it should be determined by the amount of property received by the Donee. Article 3, Regulations 79, 1936 Edition, relating to Gift Tax under the Revenue Act of 1932, is quoted in part as follows:

> "The tax is not imposed upon the receipt of the property by the Donee nor is it necessarily determined by the measure of enrichment resulting to the Donee from the transfer, nor is it conditioned upon ability to identify the Donee at the time of the transfer. On the contrary, the tax is a primary

and personal liability of the Donor, is an excise upon his act of making the transfer, **is measured by the value of the property passing from the Donor** and attaches regardless of the fact that the identity of the Donee may not then be known or ascertainable." (Emphasis supplied.)

In fact this is the identical position at one time urged by the Government. In **U. S. vs. Ryerson, et al Excrs.,** 114 Fed (2nd) 150, certiorari granted No. 495, this term the Court quoted in part from the brief of the United States as follows:

> "Under the undisputed evidence all the elements of a consummated gift were present. With respect to the donor the transfer was not **in futuro.** He thereby devised himself of all vestige of title, and no future act on his part could modify or abrogate his act. Likewise, the donees were competent to accept the gifts and they did so immeditaely. True, they were trusts, but they were no different from persons, for the Act so states. They took immediate title to and possession of all the property from the donor; they put it to instant use for the directed purpose of building up an estate for the ultimate and contingent beneficiaries, who were named specifically. The fact that those beneficiaries did not come into possession of the corpus until some time in the future, dependent upon some contingency, does not make the donor's act any the less a completed transfer to the trustees. **The fact must not be overlooked that the Act involved relates to transfers and not receipts.**"

That, according to the Court, was quoted by the United States in its brief. The exxact contrary on practically all points is now being argued by the United States in the case of **U. S. vs. Pelzer,** No. 393, this term.

The Petitioner has shifted his position so many times

as pointed out on page 14 to 17 of his brief, that it is most difficult for a taxpayer to know at any one time the position the Petitioner is taking for that moment. On page 11 of the Petitioner's brief in the Pelzer case the Petitioner makes the statement that the trust receives a present interes. This is diametrically opposed to the position taken in the case of **Charles W. Deeds vs. Commissioner**, 37 B. T. A. 293. Quoting from the Board's opinion in part:

> "The Respondent (Commissioner of Internal Revenue) claims first that the beneficiaries of the trust did not take present interest because, he argues, that possession and enjoyment of the property are postponed until a future date. This conclusion is based upon the fact that neither the property conveyed to the trust nor the income from it was as a matter of right immediately subject to the unqualified demands of the beneficiaries but rather until the beneficiaries reached the age of 30. Any distribution out of the income or principal was subect to the sole discretion of the trustee. The Respondent next claims that the transfer cannot be regarded as gifts of present interest to the trust as an entity since the trustee acquired no beneficial inerest and the gifts were not to him but to the children. He cites **Burnett vs. Guggenheim,** 288 U. S. 280, for the proposition that the Gift Tax statute is not aimed at every transfer of legal title without consideration but only at transfers that have the quality of a gift. He concludes that it is necessary to consider the equitable rather than the legal interest transferred to determine whether there was a gift of a future interest in property."

Referring again to the number of times that the Petitioner has shifted his position it may be pointed out that the Treasury Department (see Pelzer brief, page

11) in administering the gift tax proceeded for some years on the assumption that under Section 504(b) the beneficiaries of a gift in trust were considered the donees. The second position was, after several years, that while the beneficiaries were the donees, yet they took only future interests. **Deeds vs. Commissioner,** 37 B. T. A. 293. The third position taken was that the beneficiaries were not in fact the donees at all, but that the trusts or the trustees were the donees.

This last position resulted in a boomerang to the Commissioner for it clearly pointed the way to tax avoidance, and as stated in **McBrier vs. Commissioner** 108 F. (2nd) 967 was "viewed with Congressional alarm." The Court referred to the Senate Committee on Finance report for 1938 as follows:

> "The Board of Tax Appeals and several of the Federal Courts have held, with respect to gifts in trust, that the trust entities were the donees and on that account the gifts were of present and not of future interests. The statute as thus construed, affords ready means of tax avoidance, since a donor may create any number of trusts in the same year in favor of the same beneficiary with a $5,000.00 exclusion applying to each trust, whereas the gifts, if made otherwise than in trust, would in no case be subject to more than a single exclusion of $5,000.00. 75th Cong., 3d Sess. S. Rep. No. 1467, p. 41."

On page 29 of the Pelzer brief the Petitioner expresses wonder at the inconsistency of the taxpayer in that case. After reviewing the Petitioner's various positions heretofore assumed, one is inclined to agree that consistency is indeed the rarest of jewels.

It is respectfully submitted that position first taken by the Commissioner that the beneficiaries of the trust

are in fact the real donees, is the correct position.

POINT II.

The "Apprehended Difficulty" of determining the number of Donees and the amount they received is not present in this case.

The Petitioner devotes a great deal of space in his brief in the Pelzer case to what he terms the "apprehended difficulty" in determining the number and identity of the beneficiaries and the nature and value of each gift.

The Petitioner argues on page 21 of that brief that "The position that the trust should be considered as the 'person' or donee for the purpose of determining the number of exclusions is also the more practicable rule administratively since it avoids the necessity of determining the number and identity of the beneficiaries and the nature or value of their separate interest in each gift."

In this connection it may be stated that in the great majority of instances there is no difficulty in determining either fact. At least that is true in the instant case.

It may be further pointed out that the Commissioner of Internal Revenue has vast administrative powers and in all cases where it is difficult to obtain the facts in any given case, this difficulty is usually to the detriment of the taxpayer who must in each instance prove his case and relieve himself of the difficulties encountered.

It is sometimes administratively difficult to determine whether or not a bad debt is entirely worthless under the income tax statutes. It would be just as logical to attempt to invoke the aid of this Court in repeal-

ing the statute that permits a deduction for a bad debt as to appeal for a construction of the gift tax statutes that would relieve the "apprehended difficulty" of determining some given facts in some isolated cases.

It may also be stated that it is the duty of Congress to pass the administrative statutes, and if those statutes are not sufficient for the Petitioner to expediently administer the laws, then such laws should be changed by Congress, and the Petitioner should not seek to invoke the aid of the courts to legislate.

It is again stated that there is no difficulty in determining the facts in the instant case. In this case there are **seven named living beneficiaries.** (R. 9.) The value of the gift made by the donor is not in dispute, the same being $144,970.34. The beneficiaries all share and share alike. It is but a matter of simple arithmetic to determine that each **named** beneficiary, whose identity is definitely ascertainable, actually received a gift of a value in excess of $5,000.00. Otherwise there would be no tax. This notwithstanding the provision of Article 3 of Regulations 79, which states that the tax is not necessarily determined by the measure of enrichment resulting to the Donee from the transfer. Nor can it be said that the possession and enjoyment of the gift is postponed. All title and interest in the property went out of the grantor at the time of the gifts. It is upon this act of making the transfer that the excise is laid. This is the very root of the tax.

In the case of Thomas E. Wells 34 B. T. A. 315, it was there held that although **possession** of the trust property was postponed there was present **enjoyment** thereof by the beneficiaries inasmuch as it was being

administered and the income was being accumulated for their sole use and benefit. This conclusion was reached even though as in the present case the trust property was not immeditaely subject to the unqualified demands of the beneficiaries as a matter of right. This case can be said to be an even stronger case for here the beneficiaries are entitled to **all** of the income distributed by the trustees and are entitled to **all** distributions of the principal made by the trustees. They have the power of appointment under their will which is a valuable right so that even the mere exercise thereof would be a taxtable item in the estate of the deceased benficiaris. Even if one of them should die without having exercised this power of appointment the property, by the very terms of the trust vests in the heirs at law of the deceased beneficiary. If the income is not distributed it is **held** for their **use and benefit.** They alone acquired the beneficial interest. Throughout the duration of the trust the beneficiary has the sole beneficial interest which began immediately upon the creation of the trust without any beneficial interest intervening. Since this interest of the beneficiary began immediately upon the conveyance to the trust the beneficiary took a present interest in the property conveyed.

The Petitioner points out the clause in the trust instrument which is a restraint upon alienation by the beneficiaries. This clause commonly seen in trusts is known as the "spendthrift clause." The Petitioner expresses alarm over the fact that with this clause therein he may not be able to collect the tax. The Petitioner well knows that the tax is primarily an obligation of the Donor. The Donee is only secondarily liable in case the Donor either fails to pay the tax or is unable to do so.

It is true that situation could arise whereby a Donor would divest himself entirely of all of his property and thereby be wholly unable to pay the tax. The Petitioner has many remedies, however, in case the Donor cannot or will not pay the tax. Section 510 of the Revenue Act of 1932 imposes a lien upon all gifts for a period of ten years from the time the gifts are made. This lien is upon the **property.** With the Commissioner's power to restrain upon bank accounts and to levy upon property it is extremely doubtful if there has ever been any instance heretofore where the Commissioner has been unable to collect the full amount of the gift tax, at least there is nothing in the record to show that he did not. Furthermore, this so-called "spendthrift clause" or any other clause that may be written into any instrument could not prevent the collection of any tax, just and due, and of this the Petitioner well knows, yet the Petitioner in effect is asking this Court to hold in this case that the trust should be the Donee for the reason that this paragraph is included in the trust instrument. The mere fact that the holding in this case may affect many other cases appears to be of no moment to the Petitioner. In passing it may be said that it is quite apparent that this clause was not included in the trust instrument to prevent the Commissioner of Internal Revenue from collecting all tax that was just and due but was inserted therein as a protection to the beneficiaries and to the trust property against attempted assignments of the principal or income, and against judgment creditors.

If it should be held that the tax is measured by what the **Donee receives** and not what the **Donor gives,** then it would be necessary to impose the tax upon the Donee and not upon the Donor and it would be necessary to

postpone the tax until the property became subect to the Donees unqualified demands. The Petitioner's "Apprehended Difficulties" in administrative procedure would increase a thousandfold if, as the Petitioner here impliedly asserts, the value of what the **Donee receives** should be the basis of the tax. Then the difficulty of collecting from the Donee would be a complete change of both the law and the administrative procedure. This would be so entirely out of harmony with the Gift Tax Act itself that it would result in utter discord of the whole concept of the Gift Tax law as written by Congress. The Petitioner's troubles would multiply many times on account of the new angles that would be given to the new theory and the new concept in the gift tax, which would not in fact be a **gift tax** but on the other hand a **recipient taxx.** In order for the law to be in complete harmony it must be upon the basis that the tax is **upon the Donor and is not imposed upon the receipt of the property by the Donee, nor is it necessarily determined by the measure of enrichment resulting to the Donee from the transfer.**

Respectfully submitted,

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SUPREME COURT OF THE UNITED STATES.

No. 419.—October Term, 1940.

Guy T. Helvering, Commissioner of Internal Revenue, Petitioner, *vs.* Mary M. Hutchings.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Fifth Circuit.

[March 3, 1941.]

Mr. Justice Stone delivered the opinion of the Court.

The petition for certiorari presents the single question whether under § 504(b) of the Revenue Act of 1932, 47 Stat. 169, 247, the donor of property in trust for the benefit of numerous beneficiaries is entitled to a single gift tax exemption or exclusion to the extent of the first $5,000 or to separate exemptions of $5,000 for each beneficiary.

Sections 501(a), 502(1) impose for each calendar year a tax on the net amount of the transfers "by any individual . . . of property by gift". By § 501(b) the tax applies "whether the transfer is in trust or otherwise" and "whether the gift is direct or indirect". In the computation of the tax laid upon "net gifts" made during the calendar year, § 504(b) provides "In the case of gifts (other than of future interests in property) made to any person by the donor during the calendar year the first $5,000 of such gifts . . . shall not . . . be included in the total amount of gifts made during such year". And § 1111, defining generally terms used throughout the Revenue Act, provides: "(a) When used in this Act—(1) The term 'person' means an individual, a trust or estate, a partnership, or a corporation."

On December 30, 1935, the taxpayer executed a trust indenture by which she transferred, in trust, property of a value of approximately $145,000 for a term ending in 1957, unless sooner terminated by the trustees, for the benefit of her seven children, with gifts over of the share of each child in event of the death of that child before the expiration of the trust. The taxpayer in her gift tax return for 1935 excluded from the taxable amount of her gifts the sum of $5,000 for each child or a total of $35,000. The commissioner allowed only a single deduction of $5,000 in lieu of the seven

$5,000 deductions claimed by the taxpayer and assessed a deficiency accordingly. The Board of Tax Appeals, treating the trust as the donee rather than the individual beneficiaries, sustained the commissioner's assessment. The Court of Appeals for the Fifth Circuit reversed. 111 F. (2d) 229. We granted certiorari October 28, 1940, to resolve a conflict of the decision below and of like decisions in other circuits. *Welch* v. *Davidson,* 102 F. (2d) 100 (first circuit); *Rheinstrom* v. *Commissioner,* 105 F. (2d) 642 (eighth circuit); *McBrier* v. *Commissioner,* 108 F. (2d) 967 (third circuit), and in the Court of Claims, *Pelzer* v. *United States,* 31 Fed. Supp. 770, with that of the Seventh Circuit in *Ryerson* v. *United States,* 114 F. (2d) 150.

It is not doubted that separate gifts, other than of future interests, made directly to the donees without the intervention of a trustee entitle the donor under § 504(b), to one $5,000 exclusion for each gift. But the Government argues that here the trustee or the trust is the donee and as there was only a single trust there can be only a single statutory deduction from the total amount of the gifts. As the statute allows one deduction of the first $5,000 for each gift "made to any person" by the donor, the question for decision is whether in this case of a gift in trust for the benefit of the designated beneficiaries the single trust, or each beneficiary, is the "person" to whom the gift was made and for which the deduction is allowed.

The statutory definition of "person" in § 1111(a)(1) is of little aid in answering this question. The definition is made generally applicable to all of the sections of the revenue act and was carried forward from earlier acts which contained no gift tax provisions. See § 2(a)(1) of the 1926 Revenue Act, 44 Stat. 9; § 701(a)(1) of the 1928 Revenue Act, 45 Stat. 878. The section means no more than that the word "person" in any section of the act in which it occurs may be taken as meaning "trust" rather than "individual" as the context may require. But § 504(b), allowing the deduction in the case of each gift to any person when applied to gifts in trust for designated beneficiaries, may be read as referring either to a gift to the trust or a gift to each individual beneficiary. Hence we must read the section in its setting of the gift tax provisions and in the light of its legislative history, to determine whether, within its meaning, the trust or each individual beneficiary is the donee to whom the gift is made.

The gift tax provisions are not concerned with mere transfers of legal title to the trustee without surrender by the donor of the economic benefits of ownership and his control over them. A gift to a trustee reserving to the donor the economic benefit of the trust or the power of its disposition, involves no taxable gift. It is only upon the surrender by the donor of the benefit or power reserved to himself that a taxable gift occurs. *Sanford's Estate* v. *Commissioner,* 308 U. S. 39; *Rasquin* v. *Humphreys,* 308 U. S. 54, and it would seem to follow that the beneficiary of the trust to whose benefit the surrender inures, whether made at the time the trust is created or later, is the "person" or "individual" to whom the gift is made.

But for present purposes it is of more importance that in common understanding and in the common use of language a gift is made to him upon whom the donor bestows the benefit of his donation. One does not speak of making a gift to a trust rather than to his children who are its beneficiaries. The reports of the committees of Congress used words in their natural sense and in the sense in which we must take it they were intended to be used in § 504(b) when, in discussing § 501, they spoke of the beneficiary of a gift upon trust as the person to whom the gift is made. Similarly they spoke of gifts effected by transfer of money or property to another as consideration for the payment of money or other property to a third person as a gift to the third person. H. Rept. No. 708, 72d Cong., 1st Sess., pp. 27-28; S. Rept. No. 665, 72d Cong., 1st Sess., pp. 39-40. It is of some significance also that the denial by § 504(b) of the exemption in the case of gifts of "future interests" has little scope for practical operation unless the gifts to which the exemption applies include those gifts made to beneficiaries of a trust since it is by resort to the conveyance in trust that most future interests are created.

Moreover, the very purpose of allowing a gift tax exemption measured by the number of donees, would be defeated if a distinction were to be taken between gifts made directly to numerous donees and a gift made for their benefit by way of a single trust, and we are unable to discern in the statute or its legislative history any purpose to make such a distinction. While one object of the exemption was to permit small tax free gifts, and at the same time "to fix the amount sufficiently large to cover in most cases wedding and Christmas gifts" without the necessity of keeping accounts and reporting the gifts, H. Rept. *supra,* 29; S. Rept. *supra,* 41, never-

theless the statute extended the exemption in the specified amount to all gifts, whether large or small, "made to any person".

In the face of an exemption thus made broadly applicable to all gifts to all donees and in the absence of some indication of an intention to discriminate between gifts made directly to the donees and those made indirectly to the beneficiaries of a trust, we can hardly assume a purpose to favor one class of donees over the other or find such a purpose in the words of the statutory definition of "person" which may indicate either the trust or each individual beneficiary of the trust as the person to whom the gift is made. Further, such an assumption would open the way to avoid the $5,000 limitation upon the allowed exemption, by resort to the simple expedient of the creation by a single donor of any number of trusts of $5,000 each for the benefit of a single beneficiary.[1] A construction so dependent upon an artificial meaning of the words of the statute and so out of harmony with the statutory scheme and purpose is not to be favored.

Article 11 of 79 Treasury Regulations (1933 edition), issued under the 1932 Act treats each gift to the beneficiary of a trust as entitled to the benefit of the $5,000 deduction unless the gift is of a "future interest" which § 504(b) excepts from the exemption otherwise allowed. Such we think is the correct construction of the statute.

It is unnecessary to consider here the question whether a gift upon trust for impersonal, public or charitable purposes where there are no designated or ascertainable first beneficiaries is a gift to the trust entitled to a single $5,000 deduction. See *Helvering* v. *Hutchings,* 111 F. (2d) 229, 231. Nor do we consider whether the gifts to the beneficiaries here are of future interests which are excepted from the benefit of the $5,000 deduction allowed by § 504(b). That question is not presented by the petition for certiorari. But our judgment will be without prejudice to consideration of that question by the Board of Tax Appeals upon the remand to it if, under the rules and procedure governing proceedings before the Board, the Commissioner is free to present the question there.

Affirmed.

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[1] It was this construction of the statute by the Board of Tax Appeals and by "several of the federal courts" which lead to the amendment of § 504(b) so as to withdraw the exemption in the case of every gift in trust. See § 505 of the 1938 Act, 52 Stat. 447. S. Rept. No. 1567, 75th Cong., 3rd Sess., p. 41.